S&P Global Ratings

RatingsDirect®

County of Essex

November 15, 2022

This report does not constitute a rating action.

PRIMARY CONTACT

Elisa Lopez cortes
Toronto
1-416-507-2574
elisa.lopez.cortes
@spglobal.com

SECONDARY CONTACT

Adam J Gillespie
Toronto
1-416-507-2565
adam.gillespie
@spglobal.com

RESEARCH ASSISTANT

Adam Paunic
Toronto
1-6474803543
adam.paunic
@spglobal.com

Credit Highlights

Overview

Credit context and assumptions	Base-case expectations
Supportive institutions and prudent financial management practices strengthen the credit profile.	Healthy budgetary performances and liquidity will allow for continued internal funding of the county's capital plan
-- Prudent financial management underpins sustainability of the budgetary performances.	--Essex will continue to generate strong operating margins despite recent economic headwinds.
-- The County of Essex's relationship with the Province of Ontario has been stable and supportive, and we expect it will remain so.	--The county's robust after-capital surpluses and pay-as-you capital funding strategy help to mitigate debt issuances.
-- Volatility in the auto sector will hamper the recovery in employment and economic activity in the near term.	--Robust liquidity holdings will continue to bolster Essex's creditworthiness.

On June 1, 2022, S&P Global Ratings raised its ratings on the County of Essex to 'AAA' from 'AA+', following the revision of the Canadian municipal institutional framework assessment to extremely supportive and predictable from very predictable and well balanced (see "**Various Rating Actions Taken On Canadian Municipal Governments On Improved Institutional Framework Assessment**," published June 1, 2022, on RatingsDirect). The county has prudent financial management practices, and we expect it will continue to generate strong operating balances averaging 25% of operating revenues and capital surpluses averaging 15%. These surpluses will allow it to continue internally financing its capital plan, keeping the debt burden well below 30% of operating revenues in the next few years. In addition, Essex's exceptional liquidity will continue to bolster the credit profile.

Outlook

The stable outlook reflects S&P Global Ratings' expectation that, in the next two years, Essex will continue to produce very strong budgetary balances and use its pay-as-you-go strategy to finance its capital program. We also expect that its tax-supported debt burden will decline modestly to about 21% of operating revenue by 2024 while Essex maintains robust liquidity.

Downside scenario

Although we do not believe it is likely in the next two years, we could lower the rating if an external shock harms Essex's economy, leading to weakening of budgetary performance or financial flexibility such that we see after-capital balances slipping into a deficit and pushing the county's tax-supported debt to more than 30% of operating revenues.

Rationale

Robust financial practices and a supportive institutional framework are credit strengths.

Located in southwestern Ontario, Essex is composed of seven lower-tier municipalities and has a population of more than 192,700 (Census 2021). It has a beneficial location encompassing the City of Windsor, Ont. and neighboring the City of Detroit, Mich. across the Detroit River. Essex's economy is focused on the manufacturing (primarily auto) and agricultural sectors and while the latter has recently grown, the former is vulnerable to global supply issues, especially with semiconductors. Although these hindrances could gradually diminish, the global economy is reckoning with inflation and fragile demand. Consequently, unemployment in the region has remained higher than the national average through 2022. The county is making efforts to diversify its economy into more service-based sectors (including tourism, agri-business, health care and social assistance, and education), which we believe will contribute to slow-but-positive medium-term growth prospects. Essex's nominal GDP per capita will be largely in line with the national level, which we estimate to be about US$54,000 in 2022.

The county keeps disciplined financial management practices and a strong budgeting process. Essex's management team has demonstrated its ability to manage revenues and expenditures appropriately under the consolidated one-year operating budgets, which are passed annually by the council, and actual variations from budget are typically moderate. The council comprises the mayors and deputy mayors of the seven lower-tier municipalities, whose members serve four-year terms. The municipal elections took place in October 2022 with no major changes in the priorities and the management of the county.

County management is preparing some changes to its investment and asset management policies, which we expect will ensure better cost-effectiveness and flexibility for its corporate infrastructure and investment. In our opinion, financial information is sufficiently detailed and comprehensive. We also believe that debt and liquidity management is prudent and adequately risk averse.

As do other Canadian municipalities, Essex benefits from an extremely predictable and supportive local and regional government framework that has demonstrated high institutional stability and evidence of systemic extraordinary support in times of financial distress. Most recently through the pandemic, senior levels of government provided operating and transit-related grants to municipalities, in addition to direct support to individuals and businesses. Although provincial governments mandate a significant proportion of municipal spending, they also provide operating fund transfers and impose fiscal restraint through legislative requirements to pass balanced operating budgets. Municipalities generally have the ability to match expenditures well with revenues, except for capital spending, which can be intensive. Any operating surpluses typically fund capital expenditures and future liabilities (such as postemployment obligations) through reserve contributions. Municipalities have demonstrated a track record of strong budget results and, therefore, debt burdens, on average, are low relative to those of global peers and growth over time has been modest.

Strong budgetary performance will allow for continued internal funding of the capital plan without issuance of debt.

We expect Essex will continue generating robust budgetary performance in our 2020-2024 base-case forecast period, with operating balances averaging 25% of operating revenues and after-capital surpluses averaging 15% of operating revenues. To date, the county's budgetary performance hasn't deteriorated during recent economic headwinds, as revenues keep flowing and the property tax remained stable.

The county has kept a very low debt burden by internally funding its capital expenditures for many years and we do not expect it to issue any debt in the next two years. Accordingly, we forecast tax-supported debt will gradually decline to total almost C$45 million at the end of 2024, or 21% of operating revenues.

Tax-supported debt consists of debt issued on behalf of the county and Windsor incurred by the Essex-Windsor Solid Waste Authority. S&P Global Ratings recognizes that there is a lower credit risk associated with the debt on-lent to these self-supporting entities. The county's debt burden excluding the on-lent debt was 13% of operating revenues in 2021 and we believe that it will continue to decline in the next two years. In addition, tax-supported debt is less than five years of operating surpluses, which together with very low interest costs of less than 2% of operating revenues, supports our assessment of the very low debt burden. In our opinion, Essex's exposure to contingent liabilities is modest and does not represent a material credit risk.

The province has committed to building a new regional hospital complex, to be located in Windsor, by 2031. The estimated cost is C$2 billion, of which municipalities are required to fund 10%, or about C$100 million in funding provided by the county. Essex contributed capital to the dedicated reserve of C$5.8 million in 2021. The balance potentially will be covered through debt closer to the completion of the project.

Essex maintains what we consider an exceptional liquidity position through regular contributions to its reserves. We estimate that it will hold free cash and investments of about C$330 million, or enough to cover about 50x its debt service requirements in the next 12 months' debt service. Similar to that of its domestic peers, the county's access to external liquidity is satisfactory, in our view.

County of Essex Selected Indicators

Mil. C$	2019	2020	2021	2022bc	2023bc	2024bc
Operating revenue	185	196	209	200	207	212
Operating expenditure	144	145	149	153	158	164
Operating balance	42	50	61	47	48	49
Operating balance (% of operating revenue)	22.4	25.7	29.0	23.5	23.4	22.9
Capital revenue	14	9	12	13	14	14
Capital expenditure	31	32	28	30	32	33
Balance after capital accounts	25	28	45	30	31	30
Balance after capital accounts (% of total revenue)	12.6	13.6	20.2	14.0	13.9	13.3
Debt repaid	3	3	3	3	4	4
Gross borrowings	0	0	0	0	0	0
Balance after borrowings	22	25	42	27	27	26
Direct debt (outstanding at year-end)	62	59	56	53	49	45
Direct debt (% of operating revenue)	33.5	29.9	26.6	26.2	23.7	21.2
Tax-supported debt (outstanding at year-end)	62	59	56	53	49	45
Tax-supported debt (% of consolidated operating revenue)	33.5	29.9	26.6	26.2	23.7	21.2
Interest (% of operating revenue)	2.2	2.0	1.7	1.7	1.6	1.4

County of Essex Selected Indicators

Local GDP per capita ($)	--	--	--	--	--	--
National GDP per capita ($)	46,328.7	43,258.3	51,987.9	54,003.3	54,648.0	56,475.0

The data and ratios above result in part from S&P Global Ratings' own calculations, drawing on national as well as international sources, reflecting S&P Global Ratings' independent view on the timeliness, coverage, accuracy, credibility, and usability of available information. The main sources are the financial statements and budgets, as provided by the issuer. bc--Base case reflects S&P Global Ratings' expectations of the most likely scenario. C$--Canadian dollar. $--U.S. dollar.

Ratings Score Snapshot

Key rating factors	Scores
Institutional framework	1
Economy	2
Financial management	2
Budgetary performance	1
Liquidity	1
Debt burden	1
Stand-alone credit profile	aaa
Issuer credit rating	AAA

S&P Global Ratings bases its ratings on non-U.S. local and regional governments (LRGs) on the six main rating factors in this table. In the "**Methodology For Rating Local And Regional Governments Outside Of The U.S.**," published on July 15, 2019, we explain the steps we follow to derive the global scale foreign currency rating on each LRG. The institutional framework is assessed on a six-point scale: 1 is the strongest and 6 the weakest score. Our assessments of economy, financial management, budgetary performance, liquidity, and debt burden are on a five-point scale, with 1 being the strongest score and 5 the weakest.

Key Sovereign Statistics

- Sovereign Risk Indicators, Oct. 10, 2022

Related Criteria

- **General Criteria: Environmental, Social, And Governance Principles In Credit Ratings**, Oct. 10, 2021
- **Criteria | Governments | International Public Finance: Methodology For Rating Local And Regional Governments Outside Of The U.S.**, July 15, 2019
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

Related Research

- **Sector And Industry Variables | Criteria | Governments | Sovereigns: Sovereign Rating Methodology**, Sept. 28, 2022
- **Economic Outlook Canada Q4 2022: Canadian Growth To Slow On Higher Interest Rates And U.S. Weakness**, Sept. 26, 2022
- **Institutional Framework Assessment: Canadian Municipalities**, June 1, 2022
- **Various Rating Actions Taken On Canadian Municipal Governments On Improved Institutional Framework Assessment**, June 1, 2022
- S&P Global Ratings Definitions, Nov. 10, 2021

Ratings Detail (as of November 15, 2022)*

Essex (County of)	
Issuer Credit Rating	AAA/Stable/--
Senior Unsecured	AAA
Issuer Credit Ratings History	
01-Jun-2022	AAA/Stable/--
27-Nov-2017	AA+/Stable/--
29-Nov-2013	AA/Stable/--

*Unless otherwise noted, all ratings in this report are global scale ratings. S&P Global Ratings credit ratings on the global scale are comparable across countries. S&P Global Ratings credit ratings on a national scale are relative to obligors or obligations within that specific country. Issue and debt ratings could include debt guaranteed by another entity, and rated debt that an entity guarantees.